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STATE FOR WHA/BSC, WHA/EPSC, EB/TPP
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SUBJECT: PARAGUAY,S MERCOSUR DIRECTOR SKEPTICAL

REF: ASUNCION 54

Classified By: ECON Patrick R. O'Reilly for reasons 1.4 (b) and (d).

Summary

¶1. (C) Paraguay,s lead Mercosur coordinator, Didier Olmedo, shared his deep skepticism of the bloc to econoff. He criticized Mercosur as diluted by a political agenda that has evolved to the exclusion of the issues important to Paraguay: greater integration with real market access not restricted by non-tariff trade barriers (NTBs) as is the case today. Olmedo criticized Mercosur,s emphasis on trade agreements with outside parties that were generally insignificant in practical terms owing to restricted product coverage. Commenting on Paraguay,s presidency, he explained that given Mercosur,s consensus-based procedures, holding the Presidency means little in terms of setting the agenda. He was critical of the accession plans of Bolivia and Venezuela, noting that Venezuela has balked at entry requirements that are less stringent than those faced by Paraguay as an original member, and that Bolivia,s desire to be a full member of both Mercosur and the Andean Community may not be technically feasible under existing Mercosur rules. Olmedo blamed Brazil for using Mercosur as a tool to burnish its image while mismanaging the real opportunity for greater integration. Despite all the problems, though, practical considerations - including Paraguay,s landlocked status, President Duarte,s consistent public comments skeptical of globalization and free trade - suggest that the GOP will not seek serious alternatives to Mercosur any time soon. END SUMMARY.

¶2. (C) Econoff met on January 25 with Didier Olmedo, the Director General of Economic Policy at the Ministry of Foreign Affairs (MFA) and the Government of Paraguay,s chief technical level coordinator of Mercosur issues. The GOP manages its Mercosur policy on an inter-institutional basis, but Olmedo, who has the diplomatic rank of Minister, has the lead within the GOP.

Mercosur &Light8

13. (C) Olmedo was quite skeptical of Mercosur generally, commenting that it had become increasingly light and diluted with a political agenda that no longer dealt seriously with issues of integration. He said that comparing the agenda today to that from ten years ago reveals an abysmal decline in ambition in terms of true integration and movement toward a customs union. (NOTE: For Olmedo, the best long-term development solution for Paraguay would be truly unfettered market access to the bigger members of Mercosur and the integration of Paraguayan producers into the production chains of those countries. END NOTE.) The tension between Uruguay and Argentina, and between Brazil and Argentina and the latter's bypassing of internal Mercosur dispute settlement mechanisms in favor of the WTO highlight the current weakness of Mercosur institutions.

14. (C) Olmedo criticized Mercosur's emphasis on trade agreements with outside parties that were generally insignificant in practical terms owing to restricted product coverage. He mentioned South Africa, Israel, and Pakistan and attributed the outreach to Brazil's overarching desire to be seen as a leader of developing countries. For him, the agreements help Paraguay very little since agricultural exports are limited in most of them, and they distract attention from the lack of integration within Mercosur.

Presidency not Significant, if You Play Fair

15. (C) The Presidency of Mercosur lasts for six months and passes among the four founding members. Since agreement is by consensus in Mercosur and any member can propose an initiative, holding the Presidency means little in terms of setting the agenda and amounts largely to logistical burden-sharing, since the country with the Presidency is responsible for coordination of meetings, distribution of minutes and other tasks -- that is, if the country plays fair. He complained that in practice Brazil and Argentina often use the presidency to obstruct the initiatives of the other members, pretending not to have received emails or faxes and otherwise creating obstacles to initiatives about which they are unenthusiastic.

Venezuela and Bolivia

16. (C) Olmedo compared the case of Bolivia to the old Brazilian movie &Dona Flor and Her Two Husbands.8 Bolivia wants to enter Mercosur but remain part of the Andean Community, something that would be extremely difficult technically and practically and which may even be legally impossible under existing Mercosur rules. Olmedo complained that the document prepared by Brazil that proposed the acceptance of Bolivia as a full member of Mercosur was full of political prose, but barely mentioned the established legal requirements for entry. The increasingly political management of the bloc creates problems for technical experts who must try to find a way to fit political decisions into the existing technical and legal framework of Mercosur.

17. (C) The entry of Venezuela and the push to accept Bolivia create problems for Paraguay. On a personal level, Olmedo commented that Chavez is disruptive in the Summit meetings, routinely discussing issues outside the matter at hand and ignoring time limits on interventions. Olmedo also claimed that Chavez wants the rules of accession changed, despite being offered more generous terms than Paraguay had when it became part of Mercosur (e.g., in terms of the time frames for adjusting external tariffs toward the Common External Tariff, lowering tariffs applicable to Mercosur members toward zero, and acceding to other Mercosur agreements). All of which is compounded by the fact that Venezuelan requirements for import permits (and corruption, in cases where the permits have been phased out) severely limit the ability of Paraguayan firms to export to Venezuela now. He

compared Chavez to a rude patron who joins a club without paying any dues and wants the rules changed and the facilities renovated.

Asymmetries

¶18. (C) Paraguay, which represents less than one percent of Mercosur,s GDP, and Uruguay generally act in concert in seeking differential benefits from Brazil and Argentina within Mercosur. Olmedo questioned whether Uruguay, which even after its financial crisis is far wealthier than Paraguay, really deserves the same treatment as Paraguay. He also questioned what would happen if Bolivia were to become a full member, since Bolivia is already seeking similar treatment. A bloc with more &asymmetrical8 countries than normal ones inevitably would reduce any special treatment available to Paraguay.

Brazil at Fault

¶19. (C) Olmedo blamed Brazil for using Mercosur as a tool to burnish its image while mismanaging the real opportunity for greater integration. He commented that Brazil has consistently refused to allow formal discussions of non-tariff barriers (NTBs) or investment incentive schemes, which he said amount to subsidies in Brazil. A working group established in 1994 to discuss NTBs has never met. For Paraguay, NTB,s are the highest priority. There are many examples of frustrated exporters, including a first-class company (Frutika, that makes juice concentrates and exports to Germany) finding it nearly impossible to export to Brazil. A Paraguayan manufacturer of plastic drink bottles encountered obstacle after obstacle that were followed closely by the MFA as part of a bilateral working group on trade. However, after beating the company down to the point of giving up, the Brazilians finally offered investment incentives to locate production in Foz du Iguazu, the city on the Brazilian side of the Parana river across from Ciudad del Este. Olmedo said there are countless examples of such &unfair competition8 from Brazil, but Brazil refuses to systematically address the problem, offering instead piecemeal fixes that look good in the press but ultimately prove temporary and ineffective.

Lula vs. Chavez

¶10. (C) Olmedo questioned Brazil,s decision to let Chavez into the bloc, but reasoned that Lula must have calculated that it,s better to have a competitor close and perhaps exert some control. Olmedo foresees continued tension. Brazil wants a large Mercosur that it can lead and that will burnish Brazil,s standing in the world, but he said that Chavez equally wants to use Mercosur to expand his Bolivarian revolution. When Econoff pointed out that Chavez is drawing from Castro,s playbook, Olmedo agreed and said he saw considerable similarity between Chavez and Paraguay,s former dictator Alfredo Stroessner, who ostensibly held elections and passed laws, despite being very clearly a dictator. He mentioned commentary he had once seen by former Brazilian President Jose Sarney, who recalled a conversation with Stroessner many years ago in which Stroessner professed (and seemed to believe) that he had the support of the people and was doing what was best for his country. Olmedo sees clear parallels in Chavez.

COMMENT

¶11. (C) Olmedo is a seasoned diplomat whose frustration with Mercosur is both strong and well-justified. He stopped short of suggesting that Paraguay leave the bloc, and gave no

indication that the MFA or the President had any other alternative to continuing to play the hand they dealt themselves when they joined Mercosur. Practical considerations including Paraguay,s landlocked status as well as President Duarte,s consistent public comments skeptical of globalization and free trade suggest that the GOP will not seek serious alternatives to Mercosur any time soon.

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